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Ensuring Ontario's Electricity Future

2005

ONTARIO POWER AUTHORITY

Annual Report

OPA

Ontario Power Authority™

Introduction

Statement of Theme

The Ontario Power Authority (OPA) is responsible for ensuring an adequate, long-term supply of electricity for Ontario – a critical factor in the province's continued growth and prosperity, and one that affects every person and business in the province today and in the future. In pursuing and fulfilling this mandate, the OPA is committed to meeting the expectations of all its stakeholders by managing and operating responsibly, prudently and professionally.

This annual report for 2005, the first year of the OPA's operations, is intended to reflect the solid progress made by the OPA on behalf of all Ontarians.

OPA Profile

The Ontario Power Authority was established under the *Electricity Restructuring Act, 2004* and commenced operations in January, 2005. It is a not-for-profit corporation without share capital and is governed by an independent Board of Directors, with its activities and programs directed by a Chief Executive Officer. The OPA reports to the Ontario Legislative Assembly through the Minister of Energy and is licensed and regulated by the Ontario Energy Board.

In pursuit of its mandate of ensuring an adequate, long-term supply of electricity for Ontario, the OPA is structured to allow for the integration of four key activities: conservation, generation development, power system planning, and electricity sector development. Within this structure, the OPA creates and implements conservation and demand management programs, ensures adequate investment in new supply infrastructure, performs long-term electricity system planning, and facilitates the development of a more sustainable and competitive electricity system.

Information on the OPA, its mandate, structure, objectives, programs, activities and plans can be found on the website, www.powerauthority.on.ca.

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March 31, 2006

The Honourable Donna Cansfield
Minister of Energy
900 Bay Street, 4th Floor
Toronto, ON M7A 2E1

Dear Minister:

I am pleased to submit the Ontario Power Authority's 2005 Annual Report. The Report provides an overview of the OPA's activities and accomplishments during the fiscal year ended December 31, 2005, and includes the audited financial statements.

Respectfully submitted,

Peter L. Jones,
Chair

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Message from the Chair and the CEO

Peter L. Jones
Chair

Jan Carr
Chief Executive Officer

Electricity is vital to every facet of modern life and to the provincial economy. We are mindful, therefore, that the Ontario Power Authority's (OPA's) mandate, programs and activities touch on the lives of all Ontarians, since the OPA exists to ensure that adequate, long-term supplies of reliable, sustainable electrical energy remain available to them well into the future.

The OPA was created by legislation in late 2004 in recognition of the need to address electricity supply, demand and infrastructure issues in a comprehensive manner. As a not-for-profit organization with a province-wide perspective, the OPA is in a position to take a balanced view of the complexities inherent in the electricity sector, taking into account the roles of generators, distributors and transmitters, as well as the interests of users of electricity, local communities and municipalities.

Our responsibilities include building a conservation culture in Ontario, long-range electricity system planning, and ensuring adequate investment in new electricity supply infrastructure. We also have an obligation to identify innovative strategies to develop market-based approaches for meeting system needs and reducing reliance on OPA procurement contracts. This will result in initiatives which transfer the risk associated with investment in new electricity from consumers to private investors.

Since the OPA started operations in early 2005, considerable progress has been made in moving Ontario's electricity system in a positive direction. Electricity conservation program design and education initiatives are underway. The OPA has successfully completed regional electricity supply projects and a variety of new ones have been proposed and are at various stages in the implementation process. In addition, the OPA has assumed contract responsibility for other supply and demand management projects, including projects for natural gas, nuclear and renewable power generation. The OPA submitted a Supply Mix Advice Report to the Minister of Energy in December 2005, which outlined options for Ontario's electricity supply mix over the next 20-year period, with a particular emphasis on the critical activities that must be initiated within the next three years to lay the groundwork to secure our electricity future. Finally, during the early months of its corporate history, the OPA built an organization of qualified, experienced and professional people to deliver on its important mandate. In all of our 2005 activities, the OPA conducted its business in a way that allowed us to listen to and take into account the views of our many stakeholders, including community leaders, the public, customers, associations, transmission and local distribution companies, generators and investors.

Looking ahead, the 2006 Business Plan provides an overview of our planned priorities and activities in the second year of operation. Five strategic objectives determine the focus for each of the OPA's five operating groups, namely to:

- Develop, coordinate and stimulate electricity conservation and demand management;
- Develop an integrated power system plan to guide the evolution of Ontario's electricity system;

Message from the Chair and the CEO (continued)

- Facilitate needed investment in electricity system infrastructure that would not otherwise occur;
- Develop and manage retail price smoothing mechanisms and contribute to the development of a more competitive electricity system that transfers financial risk away from all electricity consumers in Ontario;
- Establish and sustain organizational capacity to achieve our strategic priorities.

Conservation and demand management are crucial to ensuring that Ontarians continue to benefit from reliable and affordable electrical power, and will continue to be a high priority for the OPA in 2006. While the Conservation Bureau made good progress in 2005, a great deal more is planned for 2006, including conservation awareness, educational initiatives and the development of a wide range of programs for residential, commercial, institutional, industrial and agricultural consumers across the province that will lead to significant, measurable savings in electricity use in Ontario. We believe that energy conservation and demand management are critical to our energy future. Our goal is to identify and support immediate, cost-effective and highly visible conservation programs that will address the public interest in contributing to the challenges facing the electricity industry, and at the same time, through sound analysis and detailed design, develop comprehensive programs which will build a conservation and demand management platform that is both economically and environmentally sustainable for the electricity system in the longer term.

The OPA will also submit an Integrated Power System Plan (IPSP) to the Ontario Energy Board in 2006. The IPSP will build on the blueprint set out in the Supply Mix Advice Report and provide additional details related to the siting of generation facilities and expansion and upgrading of the transmission system, as well as address implementation of key elements of the plan such as conservation and demand management, procurement processes, and enhancement of competition in the electricity sector. The OPA will actively seek input from a broad range of electricity stakeholders and interests across the province through consultation initiatives during the months leading up to submission of the Plan. Until the IPSP is approved, the OPA will continue, under government directives, to procure new sources of electricity supply and demand management projects to meet urgent, medium- and long-term needs across the province.

Also in 2006, the OPA will continue to pursue opportunities to lead the development of Ontario's electricity sector to a more competitive system that will reduce the financial risks to electricity consumers large and small. The OPA is working with the Independent Electricity System Operator to develop a vision of the desired end state for the evolution of Ontario's electricity system. This will be a starting point towards consultation with electricity stakeholders, establishing consensus and developing a plan to move forward. Ultimately, the goal is to have a competitive electricity system that works for the benefit of all electricity users in Ontario.

In summary, in each area of activity and responsibility covered by the OPA's mandate the organization made a solid initial contribution in 2005, while putting in place the resources and capabilities necessary to make further strong progress in 2006 and beyond. The OPA will continue to be mindful of the need for Ontarians to have critical issues relating to their electrical power supply resolved quickly, efficiently, effectively, fairly and in ways that serve their best interests today and in the future.

Review of Operations, 2005

Ensuring Ontario's Electricity Future

Ontario faces a serious electricity supply challenge as a result of increasing demand due to population and economic growth, the impending retirement of coal and nuclear facilities, and a lack of investment in new infrastructure during the past decade. To address this challenge systematically, responsibly and as a matter of high priority, the Government of Ontario established the Ontario Power Authority (OPA) in late 2004.

The OPA's fundamental purpose is to ensure a sustainable, competitive and reliable electricity system for the benefit of Ontario consumers. This includes encouraging and facilitating conservation and demand management as well as planning for and procuring adequate electricity supply from diverse sources. It also includes a responsibility to consult with the people of Ontario on this matter of critical importance to their daily lives and economic well-being.

These are responsibilities that the Board of Directors, executives and staff of the OPA take very seriously. In 2005, the OPA made a solid contribution to serving the near- and long-term interests of Ontario electricity consumers, and established a strong foundation for future progress.

Consultations with stakeholders are based on the principles of relevance, inclusiveness, accessibility, transparency and fairness.

The following section of this report describes the OPA's accomplishments in 2005, along with plans and programs in place to meet future and longer-term challenges.

Engaging Stakeholders is a High Priority

The OPA recognizes that it cannot work alone in ensuring an adequate, long-term supply of electricity. The availability of reliable and affordable electrical energy is vital to every facet of modern life—at home, at work and at the businesses, institutions and industries that serve the province.

For this reason, the OPA is committed to engaging stakeholders across as broad a spectrum as possible in its deliberations on proposed solutions to ensure electricity reliability. The 2006 Business Plan of the OPA expresses the following Guiding Principle: *"The Ontario Power Authority consults with stakeholders, including community leaders, the public, customers, associations, transmission and local distribution companies, generators and investors."*

Consultations with stakeholders are based on the principles of relevance, inclusiveness, accessibility, transparency and fairness. The OPA is also committed to continuously seeking opportunities to improve the effectiveness of its consultations through feedback from stakeholders and adopting best practices from other jurisdictions.

The OPA's consultations include individual consumers and organizations within the electricity industry as well as non-electricity industry companies, associations and special interest groups. This approach brings significant benefits to all involved – and by extension to the Ontario Energy Board (OEB) as regulators and the provincial government as policy-makers. In addition to establishing a cost-effective pool of expert knowledge, these consultations help to identify areas of potential synergy or conflict among stakeholders. For stakeholders, direct channels of communication are opened up with the OPA. This assists them in understanding OPA activities and objectives and provides opportunities for them to influence

policies early in the process and through a less formal proce lure than a regulatory hearing. In short, these c nsultations provide opportunities to build solu ion-based partnerships.

As a practica l matter, the OPA's approach to consultation will remain flexible to allow for selective stak holder engagement depending on the issue or roposed initiative at hand. The goal is to eng age the appropriate stakeholders efficiently a d effectively on an issue-by-issue basis.

The OPA un ertook a number of stakeholder engagement nitiatives in 2005. They included the York Reg on electricity supply study, centralized proc irement processes, cogeneration and combine heat and power procurement, the Supply Mix dvice Report, the Standard Offer Program an preparation of the OPA 2006 Business Pla . More details on these initiatives are provide in the following sections of this report and o the OPA website.

Conservatic a Crucial Ch Bureau is Tackling allenge

The *Electricity F structuring Act, 2004*, under which the OPA operat , provides for a Conservation Bureau with a mandate, coordination of "provide leadership in planning and and load mana easures for electricity conservation establishment ment in Ontario..." The successful direction of a C the Conservation Bureau under the the scope and ef Energy Conservation Officer and programs under iety of conservation activities and plishment of th ken represent an important accomOPA in its first year of operation.

The Government of Ontario has set two short-term conservation targets: (i) to achieve a five percent reduction in peak electricity demand in Ontario by 2007 and (ii) to achieve a 10 percent reduction in total electricity consumption by provincial government operations by 2007. The long-term objective is to create a "conservation culture" in which all Ontarians will participate by making meaningful changes in how electricity is used in homes, institutions and businesses.

To support these objectives, the Conservation Bureau is structured to focus on the residential, commercial, institutional, industrial and agricultural sectors of the Ontario economy. In each sector, research, program design and implementation, and ongoing consultation initiatives are planned and developed.

Following are some highlights of the progress made by the Conservation Bureau in 2005:

- The Conservation Fund was established to assist the many sectors of the Ontario economy by helping to fund electricity conservation and awareness projects. Priority is placed on projects that will lead to quantifiable electricity conservation and demand reductions and that can be replicated across the province. Projects funded in 2005—24 in total—related to areas as diverse as the wine, restaurant and forestry industries, small retail stores, high-rise condominiums, hospitals, schools and farms, as well as appliance exchange programs, an Energy Star program for new homes, and best practices for industrial and commercial cogeneration. A complete list of 2005 funded projects is provided on the Conservation Bureau website.
- A Certificate of Recognition program was launched to recognize those who are taking action to conserve energy in Ontario.

- The Chief Energy Conservation Officer and his staff embarked on an ambitious schedule of public speaking and communications throughout the province in order to engage interested organizations and the public in the Conservation Bureau's objectives and actions and foster the development of a conservation culture.

Progress has already been made on a number of the recommendations in the Chief Energy Conservation Officer's 2005 Annual Report.

- A number of sector-specific programs were developed and launched. For example:
  - > In November, the Bureau helped sponsor a two-day Energy Conservation Symposium at Humber College in Toronto to allow key officials in the post-secondary education sector to share ideas and best practices for incorporating energy efficiency into capital renewal projects. In addition, a readiness study was undertaken to quantify opportunities for energy conservation and efficiency across the college system.
  - > In the industrial sector, a joint initiative with the Ontario Forest Industries Association was undertaken to improve the energy efficiency of this industry, through the creation of an Energy Manager Program and other measures.
  - > In the agricultural sector, an energy benchmarking program was developed for the wine industry in collaboration with the Wine Council of Ontario.
  - > In the residential sector, the Conservation Bureau commissioned a report that assesses the key market features and cost effectiveness of a range of technologies, including space heating and cooling, lighting, water heating and domestic appliances. The report notes that electricity provides all space cooling and lighting energy and virtually all appliance power, and that space cooling (air conditioning) is critically important to peak-period loading. It also notes that significant efficiencies in "white" appliances such as refrigerators, dishwashers and ranges have been offset by greater use of other appliances such as home computers.
- Throughout 2005, the Chief Energy Conservation Officer and other Conservation Bureau staff met with local distribution companies (LDCs) and other stakeholders to build relationships and foster communications on conservation issues. The LDCs represent an important delivery channel for some of the Conservation Bureau's programs.
- In December, the Conservation Bureau commissioned a study to determine what LDCs and other organizations are doing regarding conservation to inform planning and avoid duplication with other efforts being undertaken.

In November of 2005, the Chief Energy Conservation Officer presented the Minister of Energy with his first annual report, entitled *Our Conservation Challenge*, detailing the progress made by the Conservation Bureau and outlining the plans for future programs and actions. In addition, the report makes 14 recommendations in six areas: the goals of a five percent reduction in peak demand and a 10 percent reduction in consumption by provincial operations; provincial energy policy and conservation; the *Ontario Energy Efficiency Act*; the Ontario Building Code; natural gas back-up generators; and financial incentives for hospitals and schools.

Progress has already been made on a number of the Chief Energy Conservation Officer's recommendations. For example, the Ministry of Energy is hiring additional staff to administer the *Ontario Energy Efficiency Act*; the Conservation Bureau has facilitated an agreement between the Ontario Ministry of Energy and Natural Resources Canada to study the phasing-out of T12 fluorescent lights; the Conservation Bureau is following up with the Ministry of Municipal Affairs and Housing with regard to changing the Ontario Building Code and has made pre-budget submissions to the government on introducing provincial sales tax rebates for efficient electrical appliances.

Many conservation leaders across the province have already taken steps to achieve conservation and demand management targets.

As noted in the report, electricity conservation —using less—and demand management, which relates to overall usage as well as the timing of electricity consumption, are critical to ensuring that Ontarians continue to benefit from the availability of reliable and affordable electricity, in both the near and longer terms.

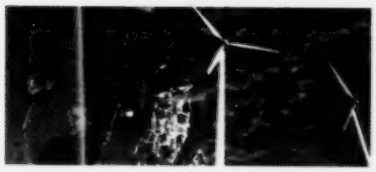
Many conservation leaders across the province have already taken steps to achieve conservation and demand management targets. Among the success stories are a "Reduce the Juice" program at Centre Dufferin District High School in Shelburne, Ontario that has helped local residents reduce electricity use by five percent; a "Doors Closed Ontario!" initiative that encourages stores and restaurants to keep their doors closed while operating air conditioning; an annual "EnergySmarts" campaign by Home Depot, the Government of Canada and the Clean Air Foundation that is the largest retail-based energy efficiency campaign in the country; a 10-megawatt Demand Response Retrofit Project by Loblaws to reduce electricity consumption during high-demand periods; an "Energy Drill" program to reduce consumption in public buildings in Milton, Ontario; and $40 million of initiatives by Toronto Hydro-Electric System Ltd. to reduce consumption by five percent, or 250 megawatts, by 2007.

In 2006, the Conservation Bureau plans to build on its activities in 2005, and in particular will focus on building a foundation for creating a culture of conservation.

Study Addresses Supply/Demand Issues in York Region

In March, 2005, the OPA began a review of electrical supply reliability issues in York Region, north of Toronto. This was an urgent and complex situation. Due to rapid residential and commercial growth, this region faces electricity supply constraints as early as the summer of 2006 and a solution was required that would meet both the physical needs and the community's expectations for involvement.

Through the spring and summer, the OPA developed and analyzed a broad range of options to meet the assessed power needs of the region. The options reviewed included conservation and demand management initiatives as well as potential new generation, distribution and transmission alternatives. In keeping with the OPA's commitment to stakeholder engagement, the process included extensive public consultation and participation in assessing options and potential solutions. A working group comprised of about 25 volunteers from the local communities, municipalities and interest groups was established, with meetings open to the general public. Two open-house public meetings



were also held to discuss preliminary findings and answer questions.

The OPA's final report was submitted to the OEB on September 30, 2005. It confirmed that the existing electrical supply infrastructure in York Region is operating at or beyond capacity and is unable to meet expected future growth in electricity demand. To cope with short-term supply issues, the OPA recommended aggressive conservation and demand management efforts in the region, along with the expansion of an existing transformer station and the installation of a new transformer station. For the longer term, it recommended construction of a natural gas-fired generating facility in the northern part of the region, along with an additional transformer station by 2011.

Since adoption of the OPA report, the OEB has directed Hydro One Networks to construct the first new transformer station in the vicinity of Holland Junction. In November, 2005, the OPA issued a draft Request for Proposals (RFP) for 20 megawatts of demand response initiatives in the York region.

The Supply Mix Advice Report envisaged a significant role for conservation, demand management and renewable energy, with strong growth in the amount of electricity supplied by renewable energy sources.

Supply Mix Advice Report Recommends Options for Future Electricity Development

In May, 2005, the Minister of Energy requested that the OPA deliver recommendations on the appropriate contributions of conservation and electricity supply from various renewable and conventional sources. In response to that request, the OPA presented the Supply Mix Advice Report to the Minister in December. The recommendations incorporated input from a range of industry and non-industry experts and stakeholders —more than 200 in total—over a six-month period. The team evaluated a range of feasible sources of electricity supply for the province against a range of potential scenarios and sensitivities, taking into account reliability, costs and financial risks, and environmental impacts.

The Supply Mix Advice Report presented 10 recommendations in three areas: conservation and demand management; renewable energy sources such as wind, hydro/waterpower, biomass and solar power; and supply sources for remaining demand including nuclear power, natural gas, and gasification of a variety of fuels, with containment of carbon dioxide. In summary, the report advised that a diversified and balanced portfolio of power sources will help to ensure the reliability and availability of electricity for Ontario over the next 20 years. It emphasized that all economic conservation potential should be pursued as a matter of priority, and it also stressed the need for flexibility to adjust to new supply and technological developments as they occur.

The report envisaged a significant role for conservation, demand management and renewable energy, with strong growth in the amount of electricity supplied by renewable energy sources. All new energy consumption growth through 2025 can be covered by conservation and demand management, while

all energy production needed to replace coal generation can be met by renewable sources and natural gas. The share of nuclear-generated power should remain the same as it is today. The diversified portfolio of power sources envisaged in the recommendations would utilize nuclear generation for base load, natural gas-fired generation for peaking and renewable technologies for energy production.

The report noted that while a combination of conservation and renewable energy should meet expected growth in electricity demand in the next 20 years, the elimination of coal and the retirement of existing nuclear facilities will require substantial investments in natural gas-fired generation and in refurbished or new nuclear capability.

The Minister of Energy released the report to the public on December 9, inviting comments by February 12, 2006. The Government also held a series of public meetings to enable further public discussion in late February 2006. Public interest has been strong, with more than 115,000 OPA website "hits" on this topic by the end of January 2006.

Ontario's electricity supply mix is at the discretion of the Government and will be prescribed to the OPA through a directive. The directive will form the basis for a 20-year Integrated Power System Plan (IPSP) to be developed by the OPA and submitted to the OEB in the summer of 2006. The IPSP will have a 20-year horizon and will be repeated on a three-year cycle. In effect, therefore, the IPSP is a "rolling" three-year action plan that can be adjusted as circumstances unfold.

Procurement Focuses on Electricity Generation and Demand-Side Projects

Under its broad mandate of ensuring adequate, long-term supply of electricity for Ontario, the OPA is charged with ensuring that there is adequate investment in both electricity generation and demand management initiatives and projects. As the OPA's Supply Mix Advice Report has noted, over the next 20 years Ontario needs to conserve, replace or rebuild some 25,000 megawatts of electricity generation capacity—a very challenging objective.

A key principle guiding the OPA's procurement role is that it will facilitate investment in generation, conservation, demand response and demand management only where that investment would not otherwise occur in the competitive market. Until the approval of the IPSP by the OEB, procurement processes are launched when the OPA is directed to do so by the Minister of Energy or the OEB.

Prior to establishing the OPA, the government sought and received proposals for new renewable energy projects and for 2,500 megawatts of new clean energy and demand-side projects. The first Request for Proposals (RFP) for renewable projects resulted in 10 projects, including landfill gas, wind power and small hydroelectric projects, for a total of 395 megawatts of power and an estimated $700 million of new investment. The second RFP for renewable proposals identified a further nine potential projects, mostly utilizing wind power, for a further 975 megawatts of power and an estimated $2 billion of new investment. A third RFP for renewable proposals is in progress.

The RFP for 2,500 megawatts of clean energy supply and demand-side project proposals issued in early 2004 led to five contracts with specific projects, including a Greenfield Energy Centre in Courtright, Ontario that will generate 1,015 megawatts of natural gas-fired power, a 570-megawatt gas-fired combined cycle facility to be built in St. Clair Township, a 280-megawatt dual gas and oil-fired combined cycle facility to be built in Mississauga, a 117-megawatt gas-fired cogeneration facility recently constructed at Pearson International Airport, and the previously mentioned 10-megawatt demand response project by Loblaws. The contracts for all of these projects are being administered by the OPA, which will also monitor the progress of the individual projects.

In June, 2005, the Minister of Energy directed the OPA to commence several procurement processes. They include up to 1,000 megawatts of new cogeneration and combined heat and power projects; up to 1,000 megawatts of urgently-needed additional supply for the Western Greater Toronto Area; and 250 megawatts of demand management and/or demand response initiatives from across the province, with particular focus on the cities of Toronto, Mississauga, Brampton and Oakville. Also, in November, 2005, the OPA issued a draft RFP for 20 megawatts of demand response initiatives in the York region.

In addition, in October, 2005, the government announced that it had reached an agreement with Bruce Power for refurbishing several units at the Bruce Nuclear facility near Kincardine, in order to add 1,500 megawatts of new base-load generating capacity from 2009 through 2036. The OPA has been directed by the Minister of Energy to assume the management of all contracts associated with this refurbishment project.

Also in October, due to looming reliability challenges at the Claireville Transformer Station in Vaughan, Ontario, the OPA was directed by the Minister of Energy to secure 874 megawatts of new gas-fired generation by negotiating directly with proponents of the Goreway Station project, which was identified by the Ministry as being the best alternative to meeting the technical and timing requirements. These negotiations were completed by the OPA in record time and the project is now under construction.

The OPA was also directed to negotiate contracts with five "early mover" generators to ensure their units remain available to replace coal-fired generation.

Standard Offer Program Will Reduce Barriers for Small Electricity Generators

In accordance with the provincial government's commitment to make greater use of cleaner sources of supply, a legislated objective of the OPA is to "facilitate diversification of sources of electricity supply by promoting the use of cleaner energy sources, including alternative and renewable sources."

Government procurement initiatives have been successful in attracting proposals for renewable energy projects that, if completed, will partially meet the government's target of having 2,700 megawatts of power generated by renewable energy by 2010. However, a number of barriers were identified which could potentially discourage the development of smaller generation projects which in aggregate could play a significant role. The identified barriers include: financial security requirements, complexity of the contracting process, the high cost of proposal development relative to larger project proponents, and overall administrative burden of the competitive RFP process.

As a result, in June, 2005, the Minister of Energy requested that the OPA and the OEB work together to develop terms and conditions for a Standard Offer Program (SOP) for smaller electricity generators that use clean or renewable sources. The objective of the SOP is to remove administrative and regulatory/contracting barriers to smaller renewable generation projects. It will provide a "standard price" that eligible generation projects will receive without the administrative burden, complex contracting and price-based competition that currently apply to all renewable-supply proposals regardless of size.

The OPA was requested to investigate the appropriate price and eligibility requirements for projects to qualify for the SOP, while the OEB was charged with focusing on necessary changes to codes and connection requirements and on ensuring non-discriminatory access to the electricity system.

In October, the OPA published a discussion paper laying out the range of issues germane to the development of a standard offer program. The paper covered the broad areas of eligibility criteria, pricing and program terms and conditions for small renewable and clean projects embedded in distribution systems. Stakeholders were then invited to attend three days of consultation sessions in mid-November to provide feedback and input. A first-day plenary session attended by some 150 stakeholders involved presentations from 25 interested parties, including associations, utilities and utility organizations, energy marketers and First Nations representatives. The remaining two days consisted of 34 one-on-one presentations commenting on the proposed SOP, including both contract and program issues.

The OPA's accomplishments in 2005 form the foundation for continued progress towards the objectives outlined in the 2006 Business Plan and, ultimately, towards ensuring Ontario's electricity future.

At the end of December, the OPA and OEB submitted a draft joint report to the Minister of Energy, outlining findings, recommendations and a proposed implementation plan.

Managing the Variance Account for the Regulated Price Plan

One of the OPA's prime responsibilities is to assist the OEB to manage a "regulated price plan" (RPP) that was established in April, 2005 by the OEB in order to provide Ontario's electricity consumers with stable, predictable prices that recover the full costs of electricity supply.

The RPP has been designed to provide stable electricity pricing so that low-volume residential and small commercial consumers, along with other designated groups such as municipalities, schools, colleges and universities, will not experience the volatility inherent in spot market prices. It is a blended average price based on the cost of electricity from Ontario Power Generation's regulated and unregulated assets as well as those of privately-owned electricity-generating entities. While prices for RPP consumers are set based upon a forecast of generating costs over the following year, it is likely that there will be a difference between these forecast costs and the actual costs of supplying electricity over the year. The OPA tracks this variance in an RPP variance account, and the difference is blended into the OEB's six-monthly calculation for the following year's prices to ensure "smooth" prices for RPP consumers. Consumers who have signed a retail contract will pay the contract price for electricity rather than the RPP price. Details of current electricity charges and variances are available on the OPA website.

Building the Organization

As 2005 was the first year of operation for the OPA, it was a year of establishing the organization and building its functional capability to meet its statutory obligations and strategic objectives.

This required identifying and hiring qualified, experienced and highly capable people and providing them with the facilities and resources needed to address the complex and challenging issues associated with electrical power supply in Ontario. From a staff of one, the Chief Executive Officer, and no office facilities or business infrastructure in January, the OPA team had expanded by year-end to 75 employees in an integrated organization with the physical resources and supporting systems in place to accomplish the tasks at hand.

2006 Business Plan Looks Ahead to Further Initiatives

In the fall of 2005, the OPA submitted its 2006 Business Plan to the Minister of Energy and the OEB. The 2006 Plan highlights the activities and initiatives that the OPA will undertake, within a framework of five strategic objectives. These are:

- Develop, coordinate and stimulate electricity conservation and demand management;
- Develop an Integrated Power System Plan to guide the evolution of Ontario's electricity system;
- Facilitate needed investment in the electricity system that would not otherwise occur;
- Manage retail price smoothing mechanisms and contribute to the development of a more competitive electricity system that transfers financial risk away from all electricity consumers in Ontario;
- Establish and sustain organizational capacity to achieve our strategic priorities.

The OPA's accomplishments in 2005 form the foundation for continued progress towards the 2006 objectives and, ultimately, towards fulfilling the critical mandate of ensuring Ontario's electricity future for the benefit of consumers and the economy.

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AUDITORS' REPORT

To the Board of Directors

We have audited the statement of financial position of the Ontario Power Authority as at December 31, 2005 and the statements of operations, cash flows and changes in net assets for the year then ended. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Authority as at December 31, 2005 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

KPMG LLP

Chartered Accountants

Toronto, Canada

February 3, 2006

KPMG LLP, a Canadian limited liability partnership is the Canadian member firm of KPMG International, a Swiss cooperative.

Statement of Financial Position

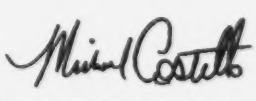
Year ended December 31, 2005

		2005
Assets		
Current Assets:		
Cash and cash equivalents	$	8,911,099
Accounts receivable, net		230,401
Other current assets (note 3)		1,871,974
		11,013,474
Regulated Price Plan Variance (note 4)	$	744,280,862
Capital assets (note 5)	$	3,394,765
	$	**758,689,101**
Liabilities and Net Assets		
Current Liabilities:		
Accounts payable and accrued liabilities	$	71,372,501
Contract deposits		84,889
Deferred rent inducement, net (note 8)		1,331,013
Due to Ministry of Energy (note 14)		6,816,692
Operating loan (note 11)		7,008,002
Revolving loan-Regulated Price Plan (note 11)		603,785,956
Retailer Settlement Balance (note 6)		72,827,345
	$	**763,226,398**
Long Term Liabilities		
Contract deposit	$	1,254,000
Net Assets		
Internally restricted for Conservation Fund (note 11)	$	1,021,250
Invested in capital assets		3,394,765
Unrestricted		(10,207,312)
		(5,791,297)
Nature of operations (note 1)		
Commitments (note 8)		
	$	**758,689,101**

See accompanying notes to financial statements.

On behalf of the Board:

Director



Director

Statement of Operations

Year ended December 31, 2005		2005
Revenues		
Fees from the IESO	$	15,000,000
Interest income		125,014
		15,125,014
Expenses		
Staff and board costs	$	5,929,823
Professional and consulting fees		6,274,558
Conservation Fund expense		78,750
General operating costs (note 7)		1,699,081
Amortization of capital assets		117,407
Income before the following:	$	1,025,395
Other Interest Income and Expense:		
Interest earned on RPP balance	$	5,969,074
Interest paid on RPP loan		(5,671,208)
Interest paid on retailers loan		(297,866)
Total Interest Income and Expense	$	–
Other Expense		
RFP costs (note 14)	$	6,816,692
Global Adjustments and Settlements		
NUG Contract	$	1[illegible]6,485,048
Generation and Conservation Programs		(1,2[illegible]1,735,249)
Global Adjustment		1,1[illegible]5,250,201
Total Global Adjustment	$	–
Excess of Expenses over Revenue	$	**(5,791,297)**

See accompanying notes to financial statements.

Statement of Changes in Net Assets

Year ended December 31, 2005

	Invested in capital assets	Internally Restricted for Conservation	Unrestricted	Total
Balance, beginning of year	$ –	$ –	$ –	$ –
Excess of expenses over revenue	(117,407)	–	(5,673,890)	(5,791,297)
Establishment of Conservation Fund	–	1,100,000	(1,100,000)	–
Conservation Fund Expenditures	–	(78,750)	78,750	–
Investment in capital assets	3,512,172	–	(3,512,172)	–
Balance, end of year	**$ 3,394,765**	**$ 1,021,250**	**$ (10,207,312)**	**$ (5,791,297)**

See accompanying notes to financial statements.

Statement of Cash Flows

Year ended December 31, 2005

		2005
Cash Flows from Operating Activities		
Excess of expenses over revenues	$	(5,791,297)
Adjustments for:		
Amortization of capital assets		117,407
Change in non-cash operating items		78,948,030
		73,274,140
Cash Flows from Financing and Investing Activities		
Advances Loan Payable to the OFA	$	603,785,956
Due to the Ministry of Energy		6,816,692
Increase in the RPP Variance Account		(744,280,862)
Increase in the Retailers Settlement Liability		72,827,345
Purchase of capital assets		(3,512,172)
		(64,363,041)
Net Increase in Cash and cash equivalents		8,911,099
Cash and cash equivalents, beginning of year		–
Cash and cash equivalents, end of year	$	**8,911,099**

See accompanying notes to financial statements.

Notes to Financial Statements Year ended December, 2005

1) Nature of Operations

The Ontario Power Authority (the "OPA" or the "Authority") was established as a non share corporation, on December 9, 2004, by the *Electricity Restructuring Act, 2004* (the "Act"). In accordance with the Act, the OPA's main objectives are:

1. To forecast electricity demand and the adequacy and reliability of electricity resources for Ontario for the medium and long term.
2. To conduct independent planning for electricity generation, demand management, conservation and transmission, and develop integrated power system plans for Ontario.
3. To engage in activities in support of the goal of ensuring adequate, reliable and secure electricity supply and resources in Ontario.
4. To engage in activities to facilitate the diversification of sources of electricity supply by promoting the use of cleaner energy sources and technologies, including alternative energy sources and renewable energy sources.
5. To establish system-wide goals for the amount of electricity to be produced from alternative energy sources and renewable energy sources.
6. To engage in activities that facilitate load management.
7. To engage in activities that promote electricity conservation and the efficient use of electricity.
8. To assist the Ontario Energy Board by facilitating stability in rates for certain types of customers.
9. To collect and provide to the public and the Ontario Energy Board information relating to medium and long term electricity needs of Ontario and the adequacy and reliability of the integrated power system to meet those needs.

The Authority's ability to continue as a going concern is dependent upon its ability to obtain financing to support operations. The OPA's credit worthiness is supported by:

(1) Legislation, which provides the OPA with a strong ability to meet its obligations.

(2) The OPA's minimal counterparty risk, given that its only counterparty will be IESO, a creation of the province and a strong counterparty.

Definitions:

OPA	Ontario Power Authority
RPP	Regulated Price Plan
IESO	Independent Electricity System Operator
NUG	Non Utility Generation
OFA	Ontario Financing Authority
RFP	Request for Proposal
OEB	Ontario Energy Board
OPG	Ontario Power Generation
LDC	Local Distribution Company
HOEP	Hourly Ontario Energy Price

2) Summary of Significant Accounting Policies

Basis of accounting:
Financial Statements are prepared in accordance with Canadian generally accepted accounting principles.

Revenue recognition:
Fees earned by the OPA are based upon OEB approved rates for electrical energy withdrawn from the IESO controlled grid by electricity consumers of Ontario. Such revenue is recognized in the period in which it is collected.

Cash and cash equivalents:
Cash and cash equivalents is comprised of bank deposit balances, term deposits and other short term investments with original maturity dates of up to 120 days.

Investments:
Market investments with maturity dates of 121 days or longer are classified as investments and valued at amortized cost. Premiums and discounts are amortized to income over the period to maturity.

Capital assets:
Capital assets are capitalized at cost. The capital cost of property and equipment is amortized on a straight line basis over their estimated service lives, as follows:

Class of Asset	Estimated Service Life
Furniture and equipment	10 years
Leasehold improvements	Over the length of lease
Computer hardware & software	2.5 years
Audio visual equipment	10 years
Telephone system	5 years

Measurement Uncertainty:
Uncertainty in the determination of the amount at which an item is recognized in the financial statements is known as measurement uncertainty. Such uncertainty exists when it is reasonably possible that there could be a material variance between the recognized amount and another reasonably possible amount, as there is whenever estimates are used. Measurement uncertainty in these financial statements exists in the valuation of the power purchase contracts and the estimated defeasance date for OPA's obligations. Estimates are based on the best information available at the time of preparation of the financial statements and will be updated annually to reflect new information as it becomes available.

3) Other Current Assets

Global adjustment recoverable	$ 1,726,149
GST recoverable	131,187
Other	14,638
Total	$ 1,871,974

4) The Regulated Price Plan Variance Account

While prices for RPP consumers are set based upon a forecast of the cost of power over the next year, it is likely that there will be a difference between the actual and forecast cost of supplying electricity to all RPP consumers.

The OPA is tracking this variance in the RPP variance account.

To assure smooth prices are provided to residential, small commercial and other designated customers, while recovering the full cost of electricity, this difference will be blended into future prices.

The following outlines the current status of the variance account:

Ontario Power Generation rebate contribution	$361,224,170
Consumer recovery contribution	377,087,619
Total RPP variance before interest	$738,311,789
Interest earned	$ 5,969,073
Total	$744,280,862

The monthly variance is shown at both a gross and net level. The gross level is the variance amount before a monthly estimate of the OPG Rebate is applied. The net level is the variance amount with the estimated OPG Rebate applied.

The result of this revenue cap is a rebate to consumers which has been named the "OPG Rebate". The actual OPG Rebate will not be known until after April 30, 2006.

Once the amount is known it will be applied to reduce the RPP variance account balance.

In order to show a more realistic variance account balance, on a monthly basis, the OPG Rebate is estimated and used to reduce the expected level of variance to be considered by the OEB in setting the next RPP price.

The RPP has been designed to provide stable electricity pricing so that consumers will not experience the volatility from electricity spot market prices.

5) Capital Assets

	Cost	Accumulated Amortization	Net Book Value
Furniture and equipment	$ 1,174,275	$ 11,021	$ 1,163,254
Leasehold improvements	1,458,998	29,275	1,429,723
Computer hardware and software	693,839	69,591	624,248
Audio visual equipment	135,843	3,436	132,407
Telephone system	49,217	4,084	45,133
	$ 3,512,172	$ 117,407	$ 3,394,765

6) Retailer Settlement Balance

Legislation provisions ensure that retailers will be held whole by the OPA for contracts with low-volume and designated consumers, entered into before prices were frozen by legislation in 2002. To ensure that retailers receive the same amounts under these contracts, the OPA and retailer settle any differences between the Hourly Ontario Energy Prices (HOEP) and the contract price. When HOEP is below the contract price, the OPA will make payments to the retailers. If the contract price is above the HOEP then the OPA receives a payment. Many of the retailer contracts that were in effect on November 11, 2002 had terms of three to five years. As a result, the number of contracts and associated volumes will decline as these contracts expire. It is expected that by November 2007, all of these contracts will have expired.

7) General Operating Costs

General program costs	$ 536,662
Information technology	101,175
Premises	551,474
Office and administration	494,483
Bank interest	15,287
Total	$1,699,081

8) Commitments

The OPA entered into a lease commitment for its office space during the fiscal year, which included various lease inducements. Deferred rent inducement represents the benefit of operating lease inducements which are being amortized on a straight-line basis over 10 years, being the term of the lease. In addition to a rent-free period until May 2006 (valued at $212,589) the OPA obtained an allowance for leasehold improvements of $1,359,332. As at December 31, 2005, the deferred rent inducement, net of amortization, was $1,331,013.

In accordance with guidance provided by the Canadian Institute of Chartered Accountants, the OPA reports an average rental cost for premises over the term of the lease agreement and amortizes the benefit of the lease inducements over the same period. As at December 31, 2005, the accrued rent liability was $3,880.

The minimum annual payments under the operating lease for the next five years are approximately as follows:

2006	$ 346,000
2007	558,000
2008	558,000
2009	575,000
2010	575,000
2011 and thereafter	3,058,000
	$ 5,670,000

9) Related Party Transactions

The OPA considers the Government of the Province of Ontario, its Agencies and its Crown Corporations to be related parties. In the normal course of operations, the OPA has transactions with the following related parties:

a) Independent Electricity System Operator (IESO)

b) Ontario Financing Authority (interest)

c) Ministry of Energy

	Revenues	**Expenses**
Independent Electricity System Operator (IESO)	$15,000,000	--
Ontario Financing Authority (interest)		$5,294,489
Ministry of Energy (RFP costs)		$ 6,816,692
	$15,000,000	$12,111,181

10) Pension Plan

The Authority makes contributions to the Ontario Pension Board, a multi-employer plan, on behalf of all staff. The plan is a contributory defined benefit plan, which specifies the amount of the retirement benefit to be received by the employees based on the length of service and rates of pay.

Contribution rates by employers are made at a rate of 8 percent of earnings; as a result, the Authority made contributions totaling $228,274 during the year.

11) Operating Loan and Revolving Loan — Regulated Price Plan

The Authority has available a revolving operating facility in the amount of $975,000,000 provided to it by the Ontario Finance Authority. The Authority used $603,785,956 by way of a promissory note with the Ontario Finance Authority to fund its payments to the IESO. The promissory note bears interest at 3.37 percent with a repayment date of January 18, 2006. The Authority also used $7,008,002 by way of a promissory note with the Ontario Finance Authority to fund its general operating expense. The promissory note bears interest at 3.40% with a repayment date of January 18, 2006.

12) Conservation Fund

The Conservation Bureau, a Division of the Ontario Power Authority, established the Conservation Fund to assist electricity conservation projects. For 2005, the OPA set up a Fund reserve of $1,100,000. During 2005, $78,750 of authorized and approved awards were paid out of the Fund.

13) Fair Value of Financial Assets and Financial Liabilities

The carrying amounts for cash, accounts receivable, loans receivable, accounts payable and accrued liabilities approximate their fair values because of the short-term maturity of these instruments.

The fair values of the Regulated Price Plan Variance, Operating loan, Revolving loan-Regulated Price Plan and Retailer settlement balance are not provided because it would not provide any additional useful information as they would be offset, and/or would not be practical to determine.

14) RFP Costs Transferred to the OPA

Under section 25.18 of the *Electricity Act, 1998*, the OPA is required to reimburse the Crown, or, if so directed by the Minister of Finance, an agency of the Crown for certain costs incurred by the Crown or an agency of the Crown after January 20, 2004 and before the Board's first approval of the OPA's procurement process under subsection 25.31(4) of the *Electricity Act, 1998*. These costs include costs incurred related to the OPA, a contract to procure supply, capacity or CDM (Conservation and Demand Management), an initiative that was commenced by the Crown that the OPA has been required to assume under a Minister's directive or a matter within the objects of the OPA.

During 2005, the OPA received two invoices from the Ministry of Energy totaling $6,816,692 for legal and consulting costs incurred for procurement contracts negotiated by the Ministry with respect to which the OPA is now the counterparty.

Corporate Information

The Ontario Power Authority is governed by an independent Board of Directors. It reports to the Ontario Legislative Assembly through the Minister of Energy, and is licensed and regulated by the Ontario Energy Board. It is managed by a Chief Executive Officer (CEO) and is comprised of five functional groups reporting to the CEO.

Board of Directors

Peter L. Jones, Chair
President, CEO and founder, Diligent Capital Inc.

Charles Bayless, Director
President of West Virginia University Institute of Technology

John M. Beck, Director
Chairman and CEO, Aecon Group Inc.

Jan Carr, Director
Chief Executive Officer, Ontario Power Authority

Louise Comeau, Director
Project Director of the Sage Climate Project at the Sage Centre and an Associate with the International Institute for Sustainable Development

Michael Costello, Director
Former President and CEO of the British Columbia Transmission Corporation and BC Hydro

Frank J. Ewasyshyn, Director*
Executive Vice President – Manufacturing, DaimlerChrysler Corporation

Richard P. Fitzgerald, Director
President and CEO of Diageo Canada

Adèle M. Hurley, Director*
President, Hurley & Associates Inc.

Ronald L. Jamieson, Director
Senior Vice-President, Aboriginal Banking, BMO Bank of Montreal

Lyn McLeod, Director
Vice-Chair and Chancellor of the Board of Governors of Confederation College and Chancellor of the University of Ontario Institute of Technology

Board Committees

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Michael Costello, Chair

Louise Comeau

Charles Bayless

Adèle M. Hurley

Frank J. Ewasyshyn

Human Resources Committee

John M. Beck, Chair

Richard P. Fitzgerald

Ronald L. Jamieson

Lyn McLeod

Corporate Officers

Peter L. Jones, Chair

Jan Carr, Chief Executive Officer

Paul Bradley, Vice President, Generation Development

Peter Love, Chief Energy Conservation Officer

Mary Ellen Richardson, Vice President, Corporate Affairs

Amir Shalaby, Vice President, Power System Planning

Paul Shervill, Vice President, Electricity Sector Development

Michael Lyle, Corporate Secretary

* *Appointed to OPA Board in March, 2006*

Corporate Contact Information

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